

Al Khalij Commercial Bank (KCBK)

Recommendation	MARKET PERFORM	Risk Rating	R-3
Share Price	QR11.80	Target Price	QR15.00
Implied Upside	+27.1%		

In-Line 1Q2019 With YoY Earnings Driven by Lower Provisions

KCBK posted 1Q2019 net income of QR176.4mn, in-line with our estimate of QR175.2mn. This result was up +4.1% YoY due to a material decline in provisions (50%). Total revenue declined YoY mainly led by a reduction in loans. However, NIM improvement was visible. Liquidity remained strong with LDR at 93%. Cost of Risk (annualized) improved to 40bps and we predict further improvement in 2019 and beyond. The upcoming market-wide 10-for-1 stock split could inject some liquidity into the name, which has historically faced thin trading volumes. We retain our Market Perform rating and QR15.00 Price Target on KCBK.

Highlights

- KCBK's 1Q2019 net income increased by 4.1% YoY on the back of a 50% drop in provisions & impairments, while total revenue exhibited weak performance.** KCBK reported net income of QR176.4mn, in-line with our estimate of QR175.2mn. The bank's revenue declined by 8.5% as a result of a drop in net interest income and lower FX revenue, the former due to a reduction in the loans and advances portfolio. Sequentially, net profit grew by 26.9% due to strong performance across the board. Given the current operating environment, we are of the view that growth in 2019's bottom-line would be driven by increase in operating income and by an improvement in CoR.
- Opex containment persisted but drop in revenue led to an uptick in C/I ratio.** Revenue declined by 8.5%, while opex receded by 4.5%. As a result, KCBK generated negative JAWS. Moreover, C/I ratio moved up to 26.8% vs. 25.7% in 1Q2018 (32.3% in 4Q2018). We do note the current efficiency ratio is acceptable and still in-line with management's target of less than 30%.
- Margins improved as the bank shed expensive deposits.** NIMs moved up by 8bps YoY and 12bps sequentially to 1.84%. It is worth mentioning that interest bearing liabilities declined by 2.0% QoQ.
- Net loans declined as management continued to shed non-core low yielding assets, targeting more lucrative deals.** Net loans contracted by 2.5% QoQ to QR30.8bn while deposits dropped by 6.4% to QR27.0bn. The drop in deposits sequentially was mainly attributed to the public sector segment. Nevertheless, KCBK's liquidity position remained strong with LDR (based on stable sources of funds) amounting to 93%.
- Asset quality remains a non-issue for now, CoR dropped.** The bank's NPLs ticked up by 1.8%, primarily driven by a drop in gross loans and interest accruing on existing NPLs. As such, the NPL ratio remained broadly stable at 1.93% vs. 1.88% at the end of 2018. Moreover, the coverage ratio (coverage of stage 3 loans/NPLs) remained flat at 82% vs. 83% in FY2018. We expect the coverage ratio to be adequately maintained as management exercises prudent risk control. CoR (annualized) also improved, receding to 46bps (in-line with our 2019 estimate) vs. 60bps in FY2018.
- Tier-1 remained robust as the bank optimized RWAs.** The bank's CET1 and Tier-1 ratios increased to 14.4% (13.0% in 2018) and 17.3% (15.6% in 2018), respectively. Moreover, KCBK ended 1Q2019 with a CAR of 18.4% (16.9% in 2018). We expect capitalization to remain robust in 2019 and the coming years.

Catalysts

- Visible progress in management's strategy:** 1) an expansion of attributable RoE beyond 12% (2019e and 2020e RoE: 10.7% and 11.1%, respectively), 2) improvement in the liquidity of the stock and 3) M&A activity.

Recommendation, Valuation and Risks

- Recommendation and valuation: We maintain our Price Target at QR15.00.** KCBK trades at P/TB and P/E of 0.7x and 6.9x on our 2019 estimates, respectively.
- Risks:** 1) Geopolitical factors/issues, 2) KCBK's market share gains do not materialize, 3) possible asset quality concerns and 4) concentration risk.

Key Financial Data and Estimates

	2018	2019e	2020e	2021e
EPS (QR)	1.54	1.71	1.86	2.09
Growth (%)	11.7	11.0	8.8	12.6
P/E (x)	7.7	6.9	6.4	5.6
TBVPS (QR)	15.09	15.95	17.04	18.33
P/TB (x)	0.8	0.7	0.7	0.6
DPS (QR)	0.75	0.75	0.75	1.00
Dividend Yield (%)	6.4	6.4	6.4	8.5

Source: Company financials, QNB FS Research; Note: All data based on current number of shares

Key Data

Current Market Price (QR)	11.80
Dividend Yield (%)	6.4
Bloomberg Ticker	KCBK QD
ADR/GDR Ticker	N/A
Reuters Ticker	KCBK.QA
ISIN	QA000A0M6MD5
Sector*	Banks & Fin. Svcs.
52wk High/52wk Low (QR)	12.43/10.55
3-m Average Volume ('000)	110.9
Mkt. Cap. (\$ bn/QR bn)	1.2/4.2
Shares Outstanding (mn)	360.0
FO Limit* (%)	49.0
Current FO* (%)	10.9
1-Year Total Return (%)	+16.1
Fiscal Year End	December 31

Source: Bloomberg (as of April 30, 2019), *Qatar Exchange (as of April 29, 2019); Note: FO is foreign ownership

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Detailed Financial Statements

Income Statement (In QR mn)	2016	2017	2018	2019e	2020e	2021e
Net Interest Income	913	984	915	943	1,026	1,129
Fees & Commissions	198	182	190	182	166	186
FX Income	31	39	38	40	42	40
Other Income	19	9	0	0	16	-2
Non-Interest Income	248	231	228	222	224	223
Total Revenue	1,160	1,215	1,143	1,165	1,250	1,352
Operating Expenses	-341	-335	-329	-330	-328	-340
Net Operating Income	819	880	814	835	922	1,012
Net Provisions & Investment Impairments	-403	-319	-190	-148	-179	-183
Net Profit Before Taxes & Non-Recurring Items	416	562	624	687	742	829
Non-Recurring Income/(Loss)	0	0	0	0	0	0
Net Profit Before Taxes	416	562	624	687	742	829
Tax	11	-11	-16	-17	-19	-21
Net Profit (Headline/Reported)	427	551	608	669	724	808
Interest Payment on Tier-1 Perpetual Note	-42	-55	-55	-55	-55	-55
Social & Sports Contribution Fund	-11	-14	-15	-17	-18	-20
Net Profit (Attributable)	374	482	538	598	651	733

Source: Company financials, QNB FS Research

Balance Sheet (In QR mn)	2016	2017	2018	2019e	2020e	2021e
Cash & Balances with Central Bank	2,359	2,587	2,881	3,724	3,351	3,871
Interbank Loans	6,489	6,617	6,100	6,517	4,357	5,530
Net Investments	15,608	12,506	10,788	11,661	10,479	9,971
Net Loans	35,180	35,094	31,636	32,688	35,476	39,238
Other Assets	620	689	219	229	248	275
Net PP&E	191	235	335	355	375	397
Goodwill & Intangible Assets	150	156	143	133	119	119
Total Assets	60,597	57,885	52,102	55,306	54,407	59,401
Liabilities						
Interbank Deposits	12,899	10,597	9,563	10,147	6,253	7,255
Customer Deposits	32,195	32,683	28,845	31,032	33,515	36,866
Term Loans	6,137	5,743	5,608	5,608	5,608	5,608
Other Liabilities	2,333	1,570	1,510	1,645	1,776	1,954
AT1 Perpetual Bond	1,000	1,000	1,000	1,000	1,000	1,000
Total Liabilities	54,564	51,593	46,526	49,432	48,153	52,684
Total Shareholders' Equity	6,033	6,292	5,577	5,874	6,254	6,717
Total Liabilities & Shareholders' Equity	60,597	57,885	52,102	55,306	54,407	59,401

Source: Company financials, QNB FS Research

Ratios/Financial Indicators	2016	2017	2018	2019e	2020e	2021e
Profitability (%)						
RoE Attributable (Based on Beg. Book Value)	6.2	8.0	8.6	10.7	11.1	11.7
RoAA (Attributable)	0.6	0.8	1.0	1.1	1.2	1.3
RoRWA (Attributable)	0.7	0.9	1.1	1.2	1.3	1.4
NIM (% of IEAs)	1.7	1.8	1.8	1.9	2.0	2.2
NIM (% of RWAs)	2.3	2.4	2.4	2.5	2.6	2.6
NIM (% of AAs)	1.6	1.7	1.7	1.8	1.9	2.0
Spread	1.5	1.4	1.5	1.6	1.6	1.6
Efficiency (%)						
Cost-to-Income (Headline)	29.4	27.6	28.8	28.3	26.3	25.2
Cost-to-Income (Core)	29.9	27.8	28.8	28.3	26.6	25.1
Liquidity (%)						
LDR	109.3	107.4	109.7	105.3	105.9	106.4
Loans/Assets	58.1	60.6	60.7	59.1	65.2	66.1
Cash & Interbank Loans-to-Total Assets	14.6	15.9	17.2	18.5	14.2	15.8
Deposits to Assets	53.1	56.5	55.4	56.1	61.6	62.1
Wholesale Funding to Loans	51.7	46.3	46.1	46.4	31.8	31.3
IEAs to IBLs	123.1	117.6	120.8	114.7	118.9	117.8
Asset Quality (%)						
NPL Ratio	1.5	1.9	1.9	1.8	1.6	1.5
NPL to Shareholder's Equity	9.0	11.1	11.0	10.6	9.2	9.2
NPLs to Tier-1 Capital	8.4	10.5	10.4	9.7	8.4	8.5
Coverage Ratio	110	118	228	238	280	283
ALL/Average Loans	1.7	2.3	4.1	4.4	4.5	4.5
Cost of Risk	103	84	60	46	48	45
Capitalization (%)						
Tier-1 Ratio	15.8	16.7	15.6	16.5	16.8	15.8
CAR	15.8	16.7	16.9	16.5	16.8	15.8
Tier-1 Capital to Assets	10.7	11.5	11.3	11.7	12.6	12.2
Tier-1 Capital to Loans	18.5	19.0	18.6	19.8	19.4	18.4
Tier-1 Capital to Deposits	20.2	20.4	20.4	20.9	20.5	19.6
Leverage (x)	10.0	9.2	9.3	9.4	8.7	8.8
Growth (%)						
Net Interest Income	(1.2)	7.9	(7.0)	3.0	8.9	10.0
Non-Interest Income	12.7	(6.9)	(1.0)	(2.8)	0.8	(0.2)
OPEX	(12.8)	(1.9)	(1.6)	0.1	(0.5)	3.6
Net Operating Income	8.8	7.5	(7.5)	2.6	10.4	9.8
Net Income (Reported/Headline)	(31.8)	29.1	10.5	10.0	8.1	11.7
Loans	5.2	(0.2)	(9.9)	3.3	8.5	10.6
Deposits	4.1	1.5	(11.7)	7.6	8.0	10.0
Assets	7.0	(4.5)	(10.0)	6.1	(1.6)	9.2
RWAs	8.8	(3.1)	(5.5)	3.9	4.6	11.7

Source: Company financials, QNB FS Research

Recommendations

Based on the range for the upside / downside offered by the 12 - month target price of a stock versus the current market price

OUTPERFORM	Greater than +20%
ACCUMULATE	Between +10% to +20%
MARKET PERFORM	Between -10% to +10%
REDUCE	Between -10% to -20%
UNDERPERFORM	Lower than -20%

Risk Ratings

Reflecting historic and expected price volatility versus the local market average and qualitative risk analysis of fundamentals

R-1	Significantly lower than average
R-2	Lower than average
R-3	Medium / In-line with the average
R-4	Above average
R-5	Significantly above average

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